ORONEGRO, INC.

IBLA 2000-289 Decided January 22, 2002

Appeal from a decision of the California State Office, Bureau of Land Management, holding five noncompetitive oil and gas leases to have expired by operation of law in the absence of any production. CAS-5118, et al.

Affirmed.

1. Oil and Gas Leases: Expiration--Oil and Gas Leases: Noncompetitive Leases

BLM properly holds that noncompetitive oil and gas leases expired by operation of law upon the conclusion of the two-year extension afforded the leases upon the termination of the unit to which they had been committed where there was no production (paying or otherwise) on the leases on the anniversary date and where the lessee had been given 60 days' notice to return wells capable of production on the leases to production but failed to do so.

APPEARANCES: Allan Rosman, President, OroNegro, Inc., Northridge, California, for OroNegro, Inc.; Emily Roosevelt, Esq., Office of the Field Solicitor, U.S. Department of the Interior, Salt Lake City, Utah, for the Bureau of Land Management.

OPINION BY ADMINISTRATIVE JUDGE HUGHES

OroNegro, Inc. (appellant), has appealed from a March 31, 2000, decision of the California State Office, Bureau of Land Management (BLM), holding five noncompetitive oil and gas leases (CAS-5118, CAS-39863-A, CAS-52689, CAS-68808, and CAS-68808-A) to have expired by operation of law at the conclusion of a two-year extension of the leases.

Three of the five leases at issue here were originally issued by BLM between September 25, 1956, and May 8, 1972, pursuant to section 17 of the Mineral Leasing Act, as amended, 30 U.S.C. § 226 (1994). 1/ They were issued to appellant's predecessor-in- interest for primary terms of 5 or 10 years, and so long thereafter as oil or gas was produced in paying quantities. The other two leases were created by BLM's approval of the partial assignment of the lessee's 100-percent record title interest in oil and gas leases CAS-39863 and CAS-68808. 2/ All of the leases were later assigned to appellant on May 18, 1994, effective April 1, 1994.

All five leases together encompass 640.04 acres in which the United States owns the subsurface (mineral) estate, situated in sec. 34, T. 27 S., R. 27 E., and sec. 2, T. 28 S., R. 27 E., Mount Diablo Meridian, Kern County, California, within the North Kern Front Oil Field (Field). The Federally-leased lands were committed (along with adjacent patented lands) to the North Kern Front Field Unit (Unit) (14-08-0001-19647 (CACA-26768-X)) effective June 1, 1982.

By decision dated October 21, 1999, the Bakersfield (California) Field Office (BFO), BLM, notified appellant that the North Kern Front Field Unit Agreement had terminated effective February 28, 1998, because of the cessation of unit production during that month and because diligent operations to restore production or discover new production had not been undertaken in the ensuing 20 months. It also stated that the five leases at issue here, all of which were then being held by unit production, would be automatically extended for a period of two years from February 28, 1998, and so long thereafter as oil or gas was produced in paying quantities, in accordance with section 17(m) of the Mineral Leasing Act, as amended, 30 U.S.C. § 226(m) (1994), and 43 CFR 3107.4. 3/ BLM further stated that failure to return the leases to production on or before February 28, 2000, would result in the expiration of the leases on that date "unless work to restore production is in progress." 4/ (Decision dated Oct. 21, 1999, at 1.)

1/ The dates of lease issuance were as follows: CAS-5118 (May 8, 1972, effective June 1, 1972), CAS-52689 (Sept. 25, 1956, effective Oct. 1, 1956), and CAS-68808 (Dec. 18, 1961, effective Jan. 1, 1962).

2/ In the case of lease CAS-39863-A, the base lease (CAS-39863) had originally been issued on Aug. 1, 1949, for a primary term of 5 years, and so long thereafter as oil or gas was produced in paying quantities, pursuant to section 17 of the Mineral Leasing Act.

3/ In the case of lease CAS-39863-A, the base lease (CAS-39863) had originally been issued on Aug. 1, 1949, for a primary term of 5 years, and so long thereafter as oil or gas was produced in paying quantities, pursuant to section 17 of the Mineral Leasing Act.

4/ We need not, in the present case, consider the accuracy of BLM's indication that the leases would not expire on Feb. 28, 2000, if work to restore production was "in progress" on that date. There is no indication that such work was in progress on that

By letter dated December 3, 1999, BFO gave appellant 60 days to take one of four courses of action with respect to each of oil and gas wells on the five leases at issue here, failing which it would be subject to civil assessments and penalties pursuant to 43 CFR Subpart 3163. 5/ BFO required appellant (1) to return each well to paying production, or, where the well is not capable of production in paying quantities, to request approval to recomplete the well in a paying zone; (2) to temporarily abandon the well, or (3) to permanently plug and abandon the well. As a fourth alternative, BFO provided that appellant could simply assign its record title interest in the lease(s) to a party willing to operate the associated wells. 6/

On December 10, 1999, BFO sent a second letter requiring appellant to provide information to BLM concerning its efforts to satisfy State requirements with respect to idle well testing and additional bonding for idle wells and to reach agreement with the private owners of the surface estate where the Federal wells are situated, with respect to indemnifying such owners and other matters. BLM had further stated that failure to comply would result in issuance of a formal shut-in order, until compliance was demonstrated.

Appellant responded to BFO's December 3, 1999, letter on December 20, 1999, stating that it was attempting to obtain the funds necessary to restart the Field and seeking an extension of time to do so: "We do not know if we can finalize a financial arrangement before the [deadline] * * *. We are working diligently on the problem and have shown that we have not deserted the leases on the field." (Letter to BLM, dated Dec. 20, 1999.) By letter dated January 7, 2000, BFO informed appellant that it would not consider appellant's request for an extension of time to comply with its December 3, 1999 letter until after appellant had complied with the information requirements set forth in the separate December 10, 1999, letter, which it was required to do prior to January 17, 2000. There was evidently no compliance, and no extension was ever granted.

Relying on information provided by BFO, the California State Office issued its March 2000 decision holding the five leases at issue here to have expired by operation of law effective February 28, 2000, in the absence of any production

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fn. 4 (continued)
date on any of the leases at issue herein.

5/ BFO's December 1999 letter was served on appellant by certified mail, return receipt requested, on Dec. 6, 1999.

6/ BLM's Dec. 3, 1999, letter is not under appeal herein.

or restoration work in progress on any of the leases. Appellant appealed from BLM's March 2000 decision.

Appellant does not dispute that, as of February 28, 2000, it was not producing any oil or gas from any of the leases at issue here. Rather, it contends that BLM erred in holding the leases to have expired and that BLM should instead have granted its request for an extension of time so that it could resume production. Appellant explains that, in the last 6 months prior to 1998 it had invested almost $1.5 million in reworking existing wells and improving field distribution and storage facilities, resulting in an increase in production from 15,000 to 30,000 barrels of oil per day. (SOR at 2.) However, it notes that, with the precipitous fall in the price of oil, it had by February 1998 "shut-in the field" and is only now on the verge of resuming production. Id. Appellant states that it now has investors ready and willing to provide the funds necessary to resume production, including a refinery which has "expressed an interest in investing with us so that they can purchase the oil produced from the field." Id. at 1. It states that, given the current price of oil, "the field is very economical to produce," concluding that "[w]e have every intention of restarting the field," and now only seek the opportunity to do so. Id. at 2.

[1] It is undisputed that the North Kern Front Field Unit Agreement terminated effective February 28, 1998, upon the cessation of production. As a result, the unitized leases were automatically extended for a period of 2 years from that date, and so long thereafter as oil or gas was produced in paying quantities. 30 U.S.C. § 226(m) (1994); 43 CFR 3107.4; Celsius Energy Co. (On Reconsideration), 154 IBLA 193, 198-99 (2001); Celsius Energy Co., 99 IBLA 53, 64, 94 I.D. 394, 400-01 (1987); see Landmark Exploration Co., 97 IBLA 96, 99 (1987); Jack L. McClellan, 34 IBLA 53, 55-57 (1978). BLM's October 1999 decision correctly so held. The lease term therefore was extended through and including February 28, 2000, and so long thereafter as oil or gas was produced in paying quantities.

There is no evidence that there was any production, paying or otherwise, on February 28, 2000, on any of the leases. 7/ Accordingly, in the absence of any provision to the contrary, the leases expired on that date.

7/ Paying production is oil and/or gas production which is sufficient in value to yield a reasonable profit after payment of all the day-to-day costs incurred following the initial drilling and equipping of the well. Abe M. Kalaf, 134 IBLA 133, 138-39 (1995). Since there was no paying production, the leases were not extended under the provisions of 43 CFR 3107.2-1.

As noted above, on December 3, 1999, BLM issued a notice requiring appellant either to put the leases in production or to take other steps. That notice demonstrates that, although there was no production, BLM deemed each of the five leases to have a well or wells capable of paying production. See Memorandum to Branch Chief, Minerals, BFO, from Chief, Division of Minerals, BFO, dated June 2, 2000, at 2 ("Upon receipt of written notice from the authorized [BLM] officer, Oro Negro, Inc. failed to restore production to any of the subject leases as stipulated in 43 CFR 3107.2-3." (Emphasis added)). Where there is a well capable of production on a lease, 43 CFR 3107.2-3 applies to condition expiration of the lease. It provides:

> No lease for lands on which there is a well capable of producing oil or gas in paying quantities shall expire because the lessee fails to produce the same, unless the lessee fails to place the lease in production within a period of not less than 60 days as specified by the authorized officer after receipt of notice by certified mail from the authorized officer to do so.

We hold that BLM's December 3, 1999, letter served as the 60-day notice provided for by 43 CFR 3107.2-3. It was sent by certified mail and received at appellant's last address of record. It clearly served to require appellant to restore production from the paying well(s), in the case of each lease, and thus provided notice "to place the lease in production" in accordance with 43 CFR 3107.2-3. There is no evidence that appellant complied with that notice. 8/ Accordingly, as lessee "fail[ed] to place the lease in production within a period of not less than 60 days as specified by" BFO's certified mail dated December 3, 1999, 43 CFR 3107.2-3 did not operate to prevent the expiration of the leases on February 28, 2000.

8/ We note that such notice was issued more than 60 days prior to the expiration date of the lease on February 28, 2000, which had been extended under section 17(m) of the Mineral Leasing Act, 30 U.S.C. § 226(m) (1994), and 43 CFR 3107.4. BLM was without authority to restrict appellant's time to restore production to any date prior to the Feb. 28, 2000, deadline. Nevertheless, the provisions of 43 CFR 3107.2-3 require a minimum of 60 days' notice. BLM simply provided a longer period of time to comply than the minimum required by the regulation.

The Dec. 3, 1999, letter also served other purposes, including serving as a courtesy notice that the 2-year extension period was soon expiring.

The question remains whether, at the conclusion of the 2-year extension provided by 30 U.S.C. § 226(m) (1994), BLM was required to provide yet another 60-day extension under 30 U.S.C. § 226(i) (1994) and 43 CFR 3107.2-2 to allow appellant to resume production. We conclude that it was not. First, the 2-year period is in lieu of the 60-day period, not in addition to it. The legislative intent of 30 U.S.C. § 226(m) was to require that, where a lease was excluded from a unit and not added to another unit, the lease must thereafter be produced, providing an adequate time of 2 years to do so. Celsius Energy Co., 99 IBLA at 71-72, 94 I.D. at 405.

Second, by its own terms, 30 U.S.C. § 226(i) (1994) does not apply in this situation. The statute provides:

> No lease issued under this section which is subject to termination because of cessation of production shall be terminated for this cause so long as reworking or drilling operations which were commenced on the land prior to or within sixty days after cessation of production are conducted thereon with reasonable diligence, or so long as oil or gas is produced in paying quantities as a result of such operations.

(Emphasis supplied.) A lease which is in an extended term under 30 U.S.C. § 226(m) (1994) and on which no production has been established is not "subject to termination because of cessation of production" at the end of its extended lease term. If there is no production, there can be no "cessation of production." 9/ 43 CFR 3107.2-2 applies only where "[a] lease * * * is in its extended term because of production in paying quantities." Leases like those under appeal are in an extended term by virtue of having been included in a unit that has been canceled, not because of production in paying quantities. Accordingly, these leases do not fall under 30 U.S.C. § 226(i) (1994) or 43 CFR 3107.2-2. 10/

9/ In other words, the extension afforded by section 17(i) of the Mineral Leasing Act and 43 CFR 3107.2–3 is restricted to a lease which has a paying well. Merit Productions, 144 IBLA 156, 158–59 (1998); Universal Resources Corp., 31 IBLA 61, 66 (1977).

10/ Of course, if production in paying quantities was established (and then ceased) during a 2-year extended term under 30 U.S.C. § 226(m) (1994), those events might bring the lease under the protection of 30 U.S.C. § 226(i) (1994), such that it could not be terminated without 60 days notice to commence reworking or drilling operations. That is not the situation here.

Appellant does not seek to take advantage of any statutory/regulatory basis for extension of its leases. Rather, it attempts to avoid the expiration of its leases by relying on the fact that it was precluded by economic circumstances from operating its lease wells and now, with the advent of favorable economic conditions, is prepared to embark on productive operations. In the absence of applicable statutory authority, BLM was unable to extend the terms of these leases regardless of appellant's economic circumstances. 11/

We therefore conclude that BLM properly held in its March 2000 decision that, in the absence of any production from or attributable to the leases, the five oil and gas leases at issue here expired by operation of law effective February 28, 2000, at the expiration of the 2-year extension of the lease following termination of the Unit to which they had earlier been committed.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the decision appealed from is affirmed.

David L. Hughes
Administrative Judge

I concur:

Will A. Irwin
Administrative Judge

11/ There is no evidence that appellant ever sought to suspend its obligation to operate and/or produce the leases, pursuant to either section 17(i) or section 39 of the Mineral Leasing Act, as amended, 30 U.S.C. § 209 (1994), and their implementing regulations, 43 CFR 3103.4–4 and 3165.1. Appellant's letter dated Dec. 20, 1999, although it requested "an extension of time," failed to set out any legal basis for such action.